

**UNITED STATES BANKRUPTCY COURT FOR THE
NORTHERN DISTRICT OF MISSISSIPPI**

IN RE:

**JAMESE AYESIA YOUNG AND
NARLESKI ARTHUR YOUNG,**

CASE NO. 07-10991-NPO

DEBTORS.

CHAPTER 13

**MEMORANDUM OPINION AND ORDER
OVERRULING THE OBJECTION TO THE PROOF OF CLAIM
OF DAISY CLAY AND
SUSTAINING THE OBJECTION OF DAISY CLAY TO CONFIRMATION OF
DEBTORS' CHAPTER 13 PLAN**

This matter came before the Court on March 26, 2008, for hearing (the “Hearing”) on the Objection to the Proof of Claim of Daisy Clay (“Objection to Proof of Claim”) (Dk. No. 100) filed by Narleski Arthur Young (the “Debtor”),¹ the Response of Daisy Clay to Debtor’s Objection to her Proof of Claim (“Response to Objection to Proof of Claim”) (Dk. No. 114) filed by Daisy Clay (“Clay”), and the Objection of Daisy Clay to Confirmation of Debtors’ Chapter 13 Plan (“Objection to Confirmation”) (Dk. No. 96) filed by Clay.² At the Hearing, Robert E. Buck represented the Debtors, W. Dean Belk represented Clay, and W. Jeffrey Collier represented Locke D. Barkley, the Chapter 13 trustee (the “Trustee”). The Court, having considered the pleadings, and the evidence

¹ Although both Debtors filed the bankruptcy case, most of the matters underlying this Memorandum Opinion and Order involve only Narleski Young. Accordingly, the Court will refer to the “Debtor” when discussing Narleski Young, and to the “Debtors” when discussing Jamese and Narleski Young.

² Although the Objection to Confirmation originally was set for hearing on February 13, 2008, no testimony was taken on that date and no evidence was presented. Rather, the Objection to Confirmation was reset to March 26, 2008, together with the Objection to Proof of Claim and Response to Objection to Proof of Claim.

and the arguments of counsel presented at the Hearing, finds that the Objection to Proof of Claim is not well taken and should be overruled, and that the Objection to Confirmation is well taken and should be sustained as follows:³

Jurisdiction

This Court has jurisdiction of the parties to and the subject matter of this proceeding pursuant to 28 U.S.C. § 1334. This matter is a core proceeding pursuant to 28 U.S.C. § 157 (b)(2)(B) and (L). Notice of the Hearing on the Objection to Proof of Claim and the Objection to Confirmation was proper under the circumstances.

Facts

The pleadings and the testimony at the Hearing established the following facts:

1. On or about October 9, 2006, Clay left her 1994 Buick LeSabre (the “Vehicle”) with the Debtor at his place of business, Kustom Care Auto (“Kustom”), for the purpose of installing new locks, a heater core, and rims.
2. On October 16, 2006, when Clay returned to Kustom to retrieve her Vehicle, the Debtor was unable to deliver the Vehicle to Clay because it apparently had been stolen from Kustom’s premises. That same day, Clay filed a police report wherein she stated her belief that the person who had sold her the Vehicle, and who had retained keys to it, had taken it from Kustom (Obj. to Conf., Ex. A).

3. On November 30, 2006, Clay filed suit against Debtor in the Circuit Court of Sunflower County, Mississippi (the “State Court”), wherein she claimed that the Debtor failed to

³ The following constitutes the findings of fact and conclusions of law of the Court pursuant to Federal Rule of Bankruptcy Procedure 7052, made applicable to contested matters by Federal Rule of Bankruptcy Procedure 9014.

properly safeguard her Vehicle. Clay sought the value of the Vehicle, together with prejudgment interest to the date of judgment, attorney fees, costs, and punitive damages (Obj. to Conf., Ex. C). The Debtor was served with a copy of the State Court Summons and Complaint on December 5, 2006 (Resp. to Obj. to Proof of Claim, Ex. C). The Debtor did not file an answer to the Complaint.

4. Accordingly, Clay filed an Application to Clerk for Entry of Default with supporting affidavit (Resp. to Obj. to Proof of Claim, Ex. E). On January 12, 2007, the State Court entered its Docket Entry of Default against the Debtor pursuant to Mississippi Rule of Civil Procedure 55(a) (“MRCP 55(a)”)⁴ Id. Clay subsequently filed an application for default judgment pursuant to MRCP 55(b).

5. On January 29, 2007, the State Court held a hearing during which Clay testified, and that same day entered a Default Judgment against the Debtor in the amount of \$21,681.06. That amount consisted of \$8,781.06 in compensatory damages, \$2,900.00 in attorney fees, and \$10,000.00 in punitive damages.

6. Clay thereafter filed a Motion for an Examination of Judgment Debtor. The State Court ordered the Debtor to appear in that court on March 26, 2007, to be examined under oath concerning his property, income, or other means for satisfying the Default Judgment. On March 19, 2007, the Debtor was served with a copy of that order (Resp. to Obj. to Proof of Claim, Ex. I). However, the Debtor did not appear in the State Court on March 26, 2007.

⁴ Hereinafter all references to the Mississippi Rules of Civil Procedure shall be defined as “MRCP.”

7. Rather, on March 26, 2007, the Debtors filed a voluntary petition pursuant to chapter 7 of the Bankruptcy Code (Dk. No. 1).⁵ In their bankruptcy schedules, the Debtors listed Clay as an unsecured nonpriority creditor holding a disputed claim in the amount of \$21,000.00⁶ (Dk. No. 14, Sch. F).

8. On November 16, 2007, the Debtors converted their chapter 7 bankruptcy case to a case under chapter 13 of the Bankruptcy Code (Dk. No. 71). The Debtors subsequently filed their proposed chapter 13 plan (the “Plan”) (Dk. No. 78). The Plan proposes zero payment to unsecured nonpriority creditors, and specifically identifies two categories of unsecured nonpriority debts: a) undisputed claims in the amount of \$2,650.00, and b) disputed claims, including Clay’s claim, in the amount of \$21,101.00.⁷

9. On January 2, 2008, Clay filed her proof of claim (the “Proof of Claim”) as an unsecured claim in the amount of \$21,681.06, based on the Default Judgment (Claims Registry, #5).

⁵ Hereinafter all code sections refer to the United States Bankruptcy Code located at Title 11 of the United States Code unless otherwise noted.

⁶ This amount actually should be \$21,681.06, based on the amount of the Default Judgment.

⁷ As observed in note 6 *supra*, this amount is incorrect because the amount of Clay’s claim should be \$21,681.06. Moreover, the “disputed” category also includes the claim of Lakeldon Redmond (“Redmond”), a creditor who has filed in this Court adversary proceeding 08-01061-NPO against the Debtor on grounds similar to those raised by Clay in her adversary proceeding 08-01049-NPO (the “Adversary”) against the Debtor. In their respective adversary proceedings, both Redmond and Clay object to discharge of their debts pursuant to § 523(a).

10. On January 17, 2008, Clay also filed her Objection to Confirmation. In her Objection to Confirmation, Clay asserts primarily⁸ that the Plan should not be confirmed because the Debtors have failed to provide for payment of the Default Judgment through the Plan.

11. On February 21, 2008, the Debtor filed his Objection to Proof of Claim wherein he states that he is not indebted to Clay because he took all reasonable measures to protect the property of his customers, and that Clay assumed the risk of the theft of the Vehicle. Further, the Debtor alleges that the Default Judgment entered against him was issued without due process of law because he did not receive notice of the State Court lawsuit or “of any and all hearings held on a writ of inquiry or related hearings on damages.” (Obj. to Proof of Claim, p. 2). Accordingly, the Debtor argues that the Default Judgment should be set aside.

12. Alternatively, the Debtor objects to the award of punitive damages against him by the State Court, arguing that punitive damages were awarded without proof of intentional or willful or wanton conduct, nor any proof of careless and reckless conduct (Obj. to Proof of Claim, p. 2). To that end, the Debtor argues that the Default Judgment should be set aside as to punitive damages, and punitive damages should be relitigated in this Court.

⁸ Clay also contends that the Debtors have not been forthcoming with the Court or creditors for reasons outlined in a Motion to Compel Debtor to Cease Business Operations and Provide Trustee with Requested Information (the “Trustee’s Motion”) (Dk. No. 35). Clay further alleges that the Debtors may not have filed certain tax returns required for confirmation of the Plan. However, the Trustee’s Motion has been resolved by the entry of an order granting the Trustee’s Motion (Dk. No. 56), and Clay failed to present evidence at the Hearing in support of either of those arguments. Moreover, as discussed *infra*, the Objection to Proof of Claim is being overruled so that Clay’s claim, subject to the ruling issued in the Adversary, will be provided the same treatment in the confirmed Plan as all other unsecured nonpriority creditors. Therefore, the Court will not address Clay’s additional bases for objecting to confirmation of the Plan.

13. In the event this Court determines that the Default Judgment is valid and the amount of punitive damages should not be relitigated, however, the Debtor concedes that he “is not opposed to reclassifying the claim from ‘disputed’ to ‘general unsecured’ to be paid the same percentage as other unsecured creditors.” (Obj. to Proof of Claim, ¶ 7).

14. On March 24, 2008, Clay filed her Response to Objection to Proof of Claim wherein she maintains that her claim should be allowed. She contends that the Debtor received adequate notice of the Default Judgment proceedings in accordance with the Mississippi Rules of Civil Procedure. Clay further asserts that the Default Judgment is a “conclusive and final adjudication of the issues necessary to justify the relief awarded and is given the same effect as a judgment rendered after a trial on the merits.” (Resp. to Obj. to Proof of Claim, p. 4). Clay also takes the position that the Debtor is precluded from relitigating the amount of punitive damages established by the Default Judgment.

Discussion

I. The State Court Lawsuit

A. Validity of the Default Judgment

1. Did the Debtor Receive the State Court Summons and Complaint?

Clay attached to the Response to Objection to Proof of Claim the proof of service by the Sunflower County Sheriff’s Department demonstrating that the Debtor was served with a copy of the State Court Summons and Complaint on December 5, 2006 (Resp. to Obj. to Proof of Claim, Ex. C). Accordingly, Clay has demonstrated that the Debtor received the Summons and Complaint and that he, therefore, was afforded due process of law.

2. Upon His Failure to Answer the State Court Summons and Complaint, was the Debtor Entitled to Notice of the Application for Default Judgment?

MRCP 55 provides:

(a) Entry. When a party against whom a judgment for affirmative relief is sought has failed to plead or otherwise defend as provided by these rules and that fact is made to appear by affidavit or otherwise, the clerk shall enter his default.

(b) Judgment. In all cases the party entitled to a judgment by default shall apply to the court therefor. If the party against whom judgment by default is sought has appeared in the action, he (or if appearing by representative, his representative) shall be served with written notice of the application for judgment at least three days prior to the hearing of such application; however, judgment by default may be entered by the court on the day the case is set for trial without such three days' notice. . . .

MRCP 55(a), (b).

The Official Comment to MRCP 55 explains:

Although an appearance by a defending party does not immunize him from being in default for failure to plead or otherwise defend, it does entitle him to at least three days written notice of the application to the court for the entry of a judgment based on his default. This enables a defendant in default to appear at a subsequent hearing on the question of damages and contest the amount to be assessed against him. Damages must be fixed before an entry of default can become a default judgment and there is no estoppel by judgment until the judgment by default has been entered.

Official Comment to MRCP 55. However, the Official Comment to MRCP 55 elaborates:

On the other hand, when a defaulting party has failed to appear, thereby manifesting no intention to defend, he not entitled to notice of the application for a default judgment under this rule.

Official Comment to MRCP 55 (emphasis added). Accordingly, the Debtor was not entitled to notice of the application for default judgment.

B. Validity of the Punitive Damages Award

1. Did the State Court Liquidate and Establish the Amount of Punitive Damages?

The Official Comment to MRCP 55 states:

When a judgment by default is entered, it is treated as a conclusive and final adjudication of the issues necessary to justify the relief awarded and is given the same effect as a judgment rendered after a trial on the merits.

Accordingly, the State Court's Default Judgment did liquidate and establish the amount of Clay's damages, including punitive damages,⁹ against the Debtor.

2. Is the Court Bound by the Amount of Punitive Damages Established by the Default Judgment for Purposes of the Bankruptcy Claims Process?

Section 502 provides:

(a) A claim or interest, proof of which is filed under section 501 of this title, is deemed allowed, unless a party in interest, . . . objects.

(b) [I]f such objection to a claim is made, the court, after notice and hearing, shall determine the amount of such claim

11 U.S.C. § 502(a), (b). As noted, Clay filed her Proof of Claim in the amount of \$21,681.06, based on the Default Judgment, and the Debtor subsequently filed his Objection to Proof of Claim. The Court thereafter conducted the Hearing at which the Debtor argued that the Default Judgment is

⁹ The Default Judgment states:

In the award of punitive damages, pursuant to Section 11-1-65, this Court has considered the following:

- a. The Defendant's financial condition and net worth;
- b. The nature and reprehensibility of the Defendant's wrongdoing;
- c. The Defendant's awareness of the amount of harm being caused;
- d. The Defendant's motivation in causing such harm;
- e. The duration of Defendant's misconduct; and
- f. Awareness that the Defendant attempted to commit such misconduct.

subject to collateral attack on the issue of punitive damages because Clay failed to prove in the State Court action that punitive damages should be awarded. The Debtor, however, failed to present any evidence or legal authority in support of its position. Clay argued at the Hearing that the State Court litigated and reduced to judgment the amount of damages owed to her, and that this Court is bound to give effect to the Default Judgment.

This Court finds that it is precluded from relitigating the amount of punitive damages.¹⁰ The Court of Appeals for the Fifth Circuit has stated that “[i]n deciding the preclusive effect of a state court judgment in federal court . . . we must look to the state court that rendered the judgment to determine whether the courts of that state would afford the judgment preclusive effect.” Gober v. Terra + Corp. (In re Gober), 100 F.3d 1195, 1201 (5th Cir. 1996).¹¹ Given that the Default Judgment was issued by a Mississippi state court, this Court will look to Mississippi’s law regarding the preclusive effect of a prior judgment.

The elements of res judicata, applied under Mississippi law, are present in this case: (1) the parties to the State Court Default Judgment are the same as the parties to this action; (2) the State Court had jurisdiction to enter the Default Judgment; (3) the Default Judgment was a final judgment on the merits; and, (4) the Default Judgment resolved the same claim that the Debtor now seeks to challenge, *i.e.*, the amount of punitive damages. See Moore v. Jones County School Dist., 239 Fed.

¹⁰ Although the Court will give preclusive effect to the Default Judgment for purposes of the bankruptcy claims process, it makes no finding that it will give the Default Judgment the same preclusive effect for purposes of the dischargeability issues raised in the Adversary.

¹¹ The Gober case elaborates that “[t]he rule of issue preclusion, or collateral estoppel, bars relitigation of issues that were actually litigated and decided in a previous action” while claim preclusion or res judicata “describe[s] the effect of a prior judgment on all legal theories and claims that should have been advanced in connection with a particular cause of action.” In re Gober, 100 F.3d at 1200, n. 2.

Appx. 913 (Miss. 2007) (delineating elements of res judicata); *see generally* Franklin Collection Serv., Inc. v. Stewart, 863 So.2d 925, 929 (Miss. 2003) (“A judgment by default is given the same effect as if a verdict was entered for the plaintiff and accordingly can have preclusive effect on other litigation.”); *see also* Bloomer v. Bustraan, 32 B.R. 25 (Bankr. W.D. Mich. 1983) (res judicata defeats objection to claim based on prebankruptcy state court default judgment in absence of fraud or collusion). Consequently, this Court should give preclusive effect to the amount of punitive damages established by the Default Judgment rendered in the State Court. Accordingly, the Objection to the Proof of Claim should be overruled, and the Proof of Claim should be allowed as an unsecured nonpriority claim in the amount of \$21,681.06.¹²

II. The Chapter 13 Case

In the Objection to Confirmation, Clay states that the Debtors propose to pay all unsecured debts except for the Default Judgment (Obj. to Conf., p. 2). The Debtors did, in fact, dispute Clay’s claim and exclude it from payment through the Plan. However, the parties agreed at the Hearing that if the Objection to Proof of Claim was not sustained, Clay’s claim should be classified as an undisputed claim and treated as all other unsecured nonpriority claims for Plan purposes. Accordingly, the Objection to Confirmation should be sustained, and the Plan should be confirmed with Clay’s claim treated as all other unsecured nonpriority claims.¹³

Conclusion

Based on the foregoing, the Objection to Proof of Claim should be overruled, and the Proof of Claim should be allowed as an unsecured nonpriority claim in the amount of \$21,681.06.

¹² Subject to the decision rendered in the Adversary.

¹³ *See* note 12.

Moreover, the Objection to Confirmation should be sustained, and the Plan should be confirmed with Clay's claim treated as all other unsecured nonpriority claims, subject to Plan modification based upon the decision rendered in the Adversary, which will be set for hearing by separate order.

IT IS, THEREFORE, ORDERED that the Objection to Proof of Claim is overruled, and that the Proof of Claim shall be allowed as an unsecured nonpriority claim in the amount of \$21,681.06.

IT IS FURTHER ORDERED that the Objection to Confirmation is sustained, and that the Plan shall be confirmed with Clay's allowed claim treated as all other unsecured nonpriority claims.

SO ORDERED, this the 9th day of May, 2008.

/ s / Neil P. Olack

NEIL P. OLACK

UNITED STATES BANKRUPTCY JUDGE